

# Investment Office Roadmap Cost Effectiveness and Financial Overview Update for the Investment Committee Janine Guillot, COIO

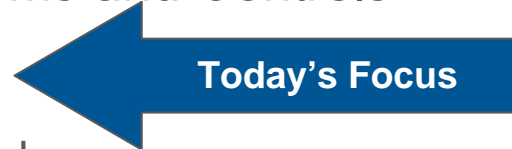
March 14, 2011

# Background & Purpose

- Provide an update on the Cost Effectiveness Roadmap Priority
- Educate the Investment Committee regarding various components of Investment Office expenses
- Update the Investment Committee on how we compare to key industry benchmarks

# Roadmap Objectives

- The 2011-12 Roadmap consists of six strategic priorities:
  - Investment Performance
  - Capital Allocation
  - Risk Management
  - Organization Systems and Controls
  - Cost Effectiveness
  - Talent Management
- Cost Effectiveness Objective: Enhance cost effectiveness of the investment program to improve net returns on assets



# Cost Effectiveness Vision

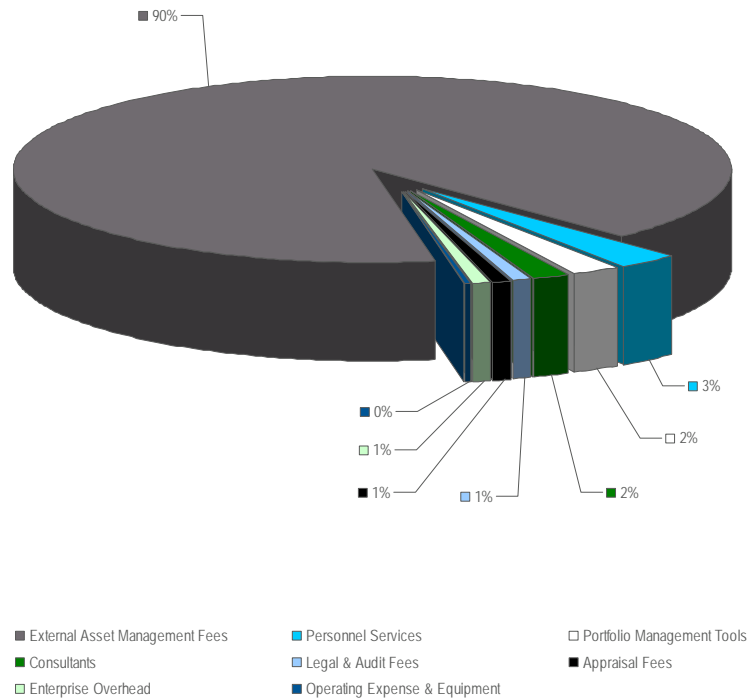
Cost Effectiveness Today (FROM)	(TO) Vision
Limited cost awareness and governance at Asset Class level and organization level	More sophisticated financial management and governance structure that ensures pervasive cost awareness at asset class and organization level
Inadequate reporting systems and data for effective cost management	Better tracking and reporting systems and improved data management
Siloed budget structure; individual asset class allocation of resources	Coordinated budget and resource allocation across INVO, within the context of INVO's overall priorities
Lack of flexibility to drive best cost/ value proposition	Greater flexibility to manage resources in the best interest of the fund and improved decision making regarding use of internal vs. external resources
Difficult to compare cost performance against relevant peers	Outperformance of relevant peers per unit of value

# Cost Effectiveness Initiatives for 2011-12

- Continue external fee reduction initiatives
- Design enhanced financial reporting materials at the asset class and total fund level
- Develop financial reporting tools and capabilities to manage and track expenses
- Provide integrated Total Fund financial reporting across investment and administrative expenses
- Identify a relevant peer group and process by which to benchmark total expenditures, work with CEM to refine benchmark data collection and to make it actionable

# Investment Office Total Expenses<sup>1</sup>

FY 2009 – 10: \$1.2 Billion

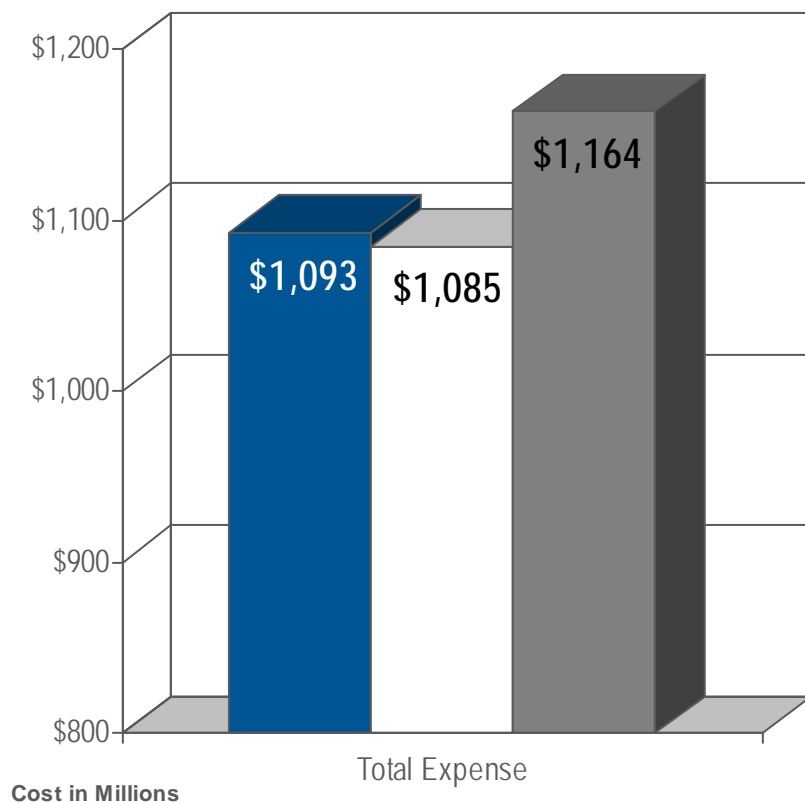


Expense Category	% of Total Expenses
External Asset Management Fees	90%
Personnel Services	3%
Portfolio Management Tools	2%
Consultants	2%
Legal & Audit Fees	1%
Appraisal Fees	1%
Enterprise Overhead	1%
Operating Expense & Equipment	0%

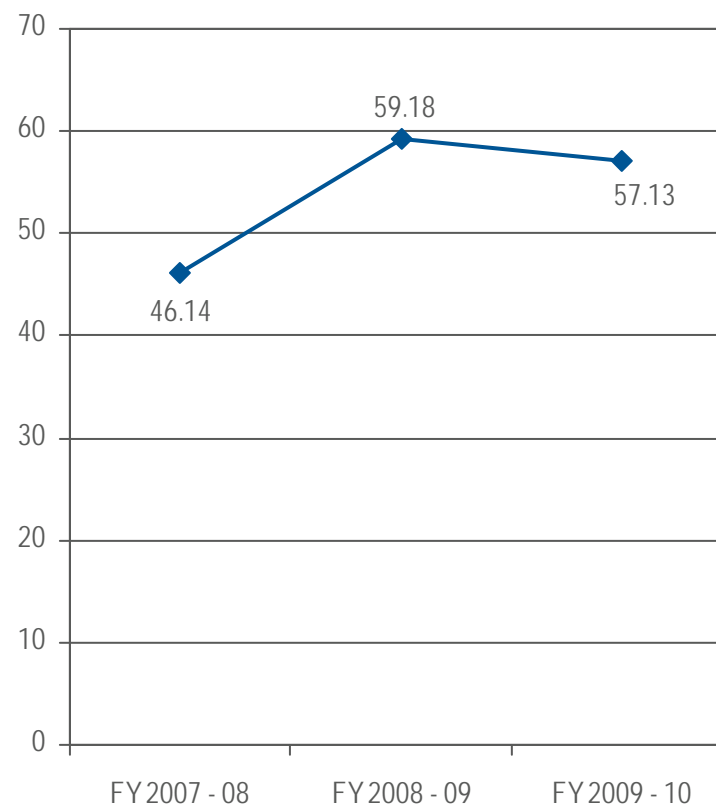
# Investment Office Total Expenses

Funding Source	Category	\$	Description
Investment Expense	External Asset Management Fees	\$1,055,802,000	Base and performance fees
Administrative Budget	Personnel Services	\$29,501,000	Permanent, retired annuitant, and student salaries and wages, retirement, and benefits, and incentive compensation
Investment Expense	Portfolio Management Tools	\$26,204,000	Custodial fees and investment tools, data, and technology (e.g., BlackRock, IFS, FactSet, Bloomberg, Charles River)
Investment Expense	Consultants	\$19,166,000	Investment consultant costs including Board and Spring Fed Pools
Investment Expense	Legal & Audit	\$11,098,000	
Investment Expense	Appraisal Fees	\$10,398,000	
Investment Expense	Enterprise Overhead	\$10,332,000	Other division/branch costs including facilities and enterprise wide expenses
Administrative Budget	Operating Expense & Equipment	\$1,636,000	Travel, communication, training, and executive search expenses
Grand Total		\$1,164,137,000	

# Investment Office 3 Year Cost Trend<sup>2</sup>



■ FY 2007 - 08 □ FY 2008 - 09 ■ FY 2009 - 10

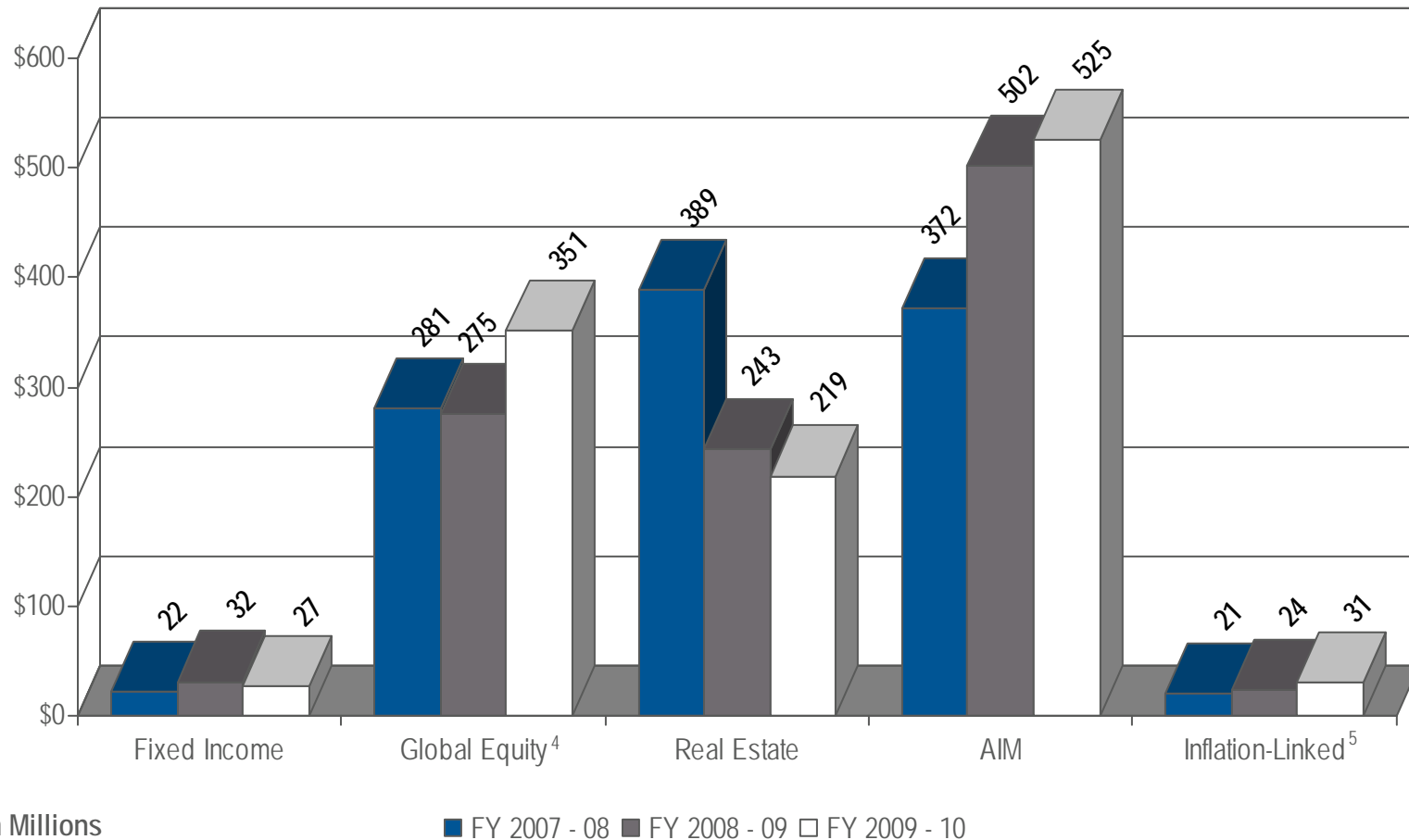


◆ Total Expense as a % of Assets (Basis Points)



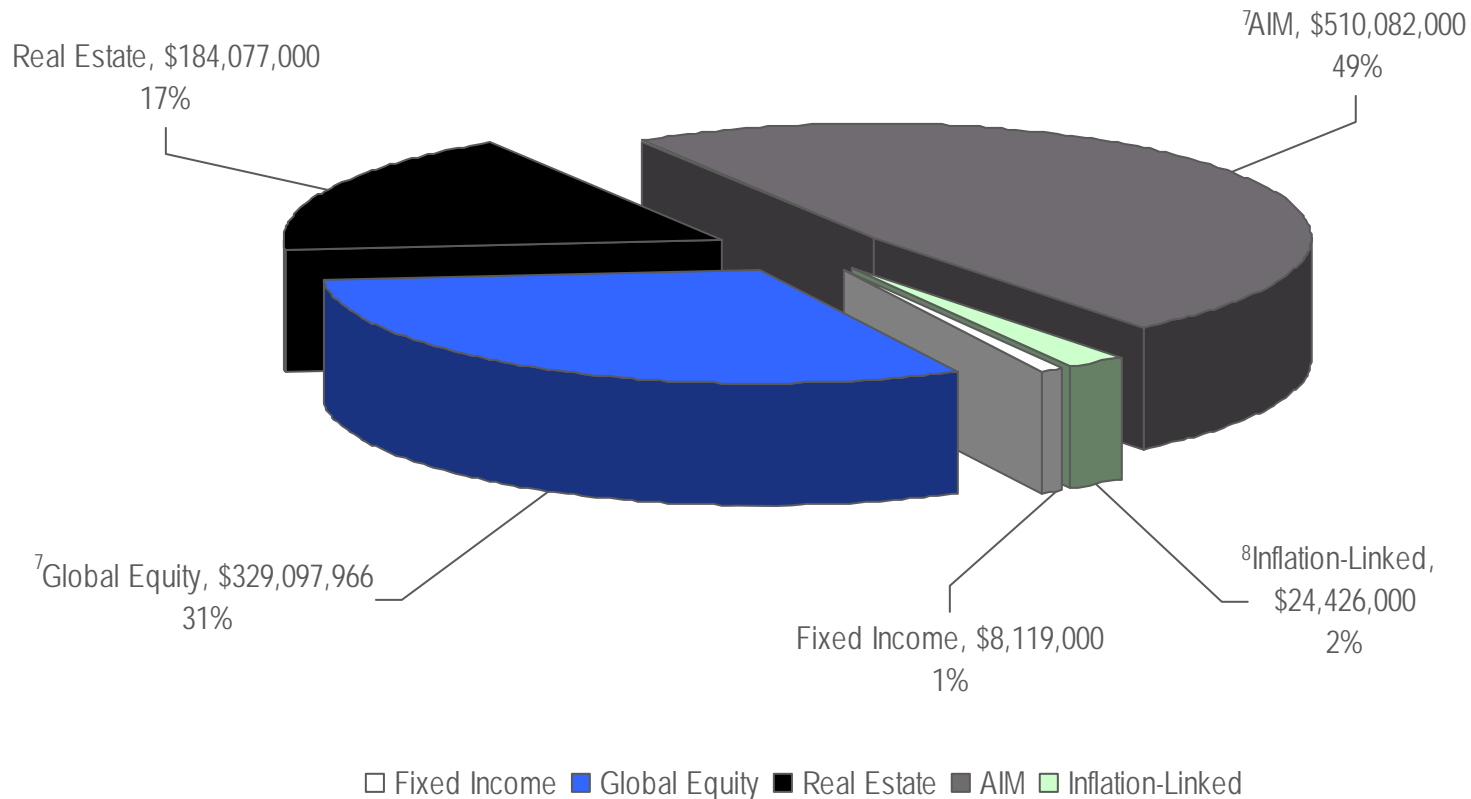
# Total Annual Costs by Asset Class<sup>3</sup>

## 3 FY Comparison - Estimated



# External Asset Management Fees by Asset Class<sup>6</sup>

FY 2009 - 10



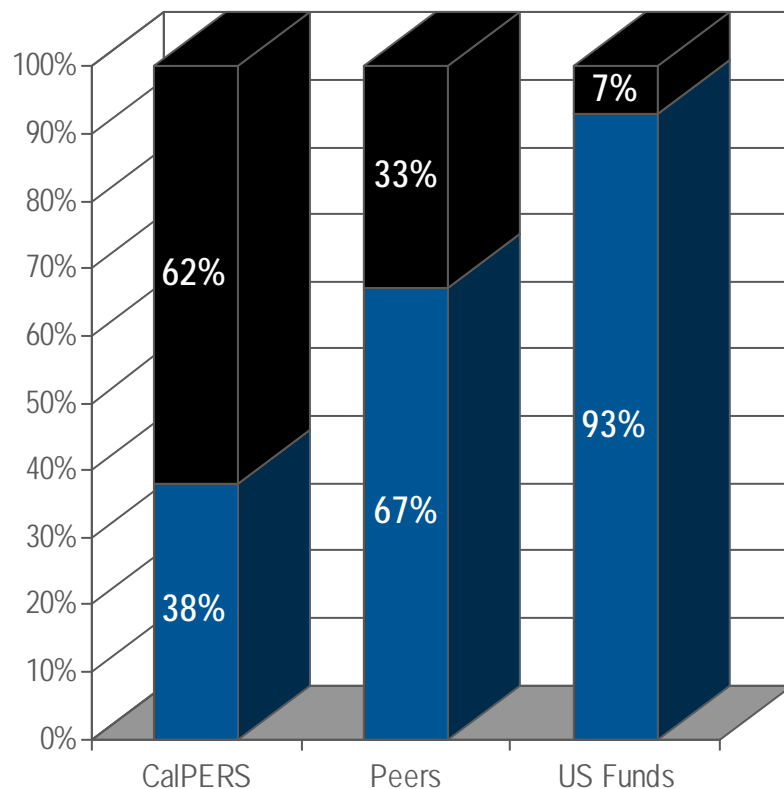
## CalPERS Total Cost Compared to CEM Benchmarks<sup>9</sup>

	\$	Basis Points
CalPERS Actual Cost	\$1,077,762,000	55.8 bps
CalPERS Benchmark Cost	\$1,234,335,000	63.9 bps
<b>CalPERS Cost Advantage</b>	<b>(\$156,573,000)</b>	<b>(8.1) bps</b>

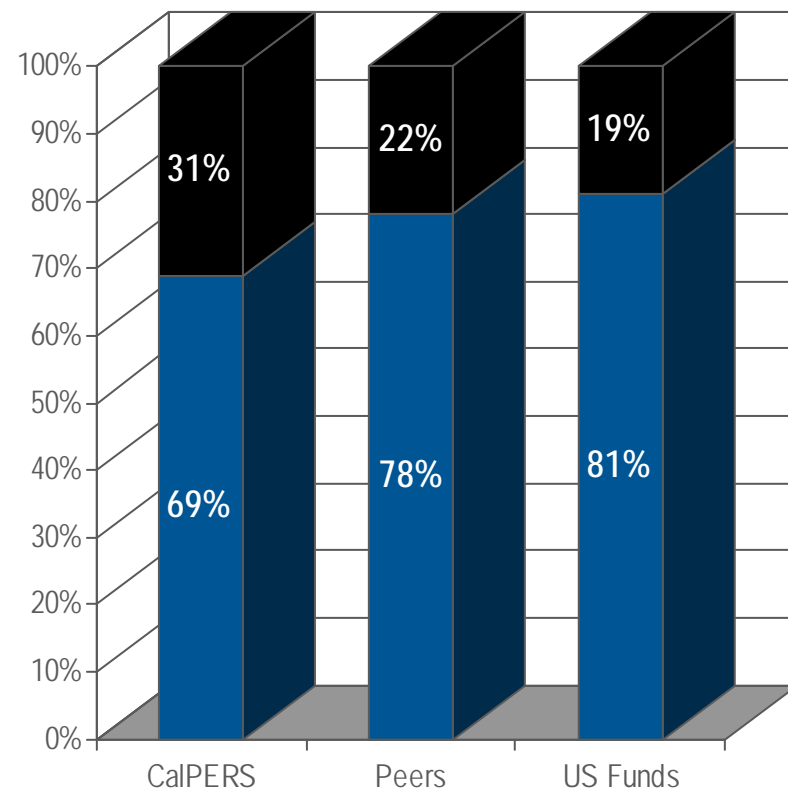
- CalPERS is relatively low cost compared to CEM Benchmarks.
- CEM Custom Peer Group for CalPERS: 10 sponsors with AUM between \$45.6 B and \$134.1 B; Median size \$64.5 B vs. CalPERS \$203.3 B.
- Benchmark cost is computed as an estimate of what our cost would be given our actual asset mix and the median costs that our peers pay for similar services. It represents the cost our peers would incur if they had CalPERS actual asset mix.
- CalPERS Cost advantage is primarily driven by public markets implementation style.

## CalPERS Implementation Style vs. Peers<sup>10</sup>

CalPERS manages more assets internally and more assets passively than peers, resulting in a significant cost advantage



■ Externally Managed ■ Internally Managed



■ Actively Managed ■ Passively Managed

# CEM Benchmark for Private Assets

- The costs for Private Assets are the most difficult to benchmark because differences are often due to variances in program style, maturity, and accounting treatment for rebates instead of true savings.
- CEM neutralized the effect of our costs for Private Equity and Real Estate. The median costs were set equal to CalPERS costs in total fund analysis.
- CEM did provide some private asset cost data as information.
  - Private Equity - CalPERS 82.3 bps vs. 165.0 bps for the group of funds that provided detailed costs.
  - Real Estate - CalPERS 53.3 bps vs. 106.0 bps reported for our peers.

## Next Steps

- Develop external fee reduction target for 2011 – 12
- Execute 2011 – 12 Roadmap Initiatives
  - Enhance financial reporting automation and data integrity
  - Determine appropriate Benchmarks to set expense ratio targets for the Fund
- Report progress quarterly through Roadmap updates
- Provide periodic financial reporting to the Investment Committee
  - Synchronize Fiscal and INVO reporting

# APPENDIX

- Consultant Expenses, FY 2009 – 10
- External Asset Management Expenses, FY 2009 – 10

# Consultant Expenses: 2009 – 10<sup>11</sup>

Consultant	\$	% of Total Consultant Expenses
PCA (Real Estate, AIM, and General Pension)	\$4,861,000	25.36%
LP Capital (AIM)	\$3,328,000	17.36%
Wilshire Associates (Total Fund)	\$2,861,000	14.93%
Le Plastier (Real Estate)	\$1,343,000	7.01%
Bard (Real Estate)	\$1,006,000	5.25%
Remaining Investment Consultants <sup>12</sup>	\$5,767,000	30.09%
<b>Grand Total</b>	<b>\$19,166,000</b>	<b>100%</b>



## External Asset Management Expenses: Top 5 by Asset Class (2009 – 10<sup>12</sup>)

Asset Class	External Manager/Partner	\$
AIM <sup>13</sup>	Carlyle Group	\$52,450,000
	TPG	\$35,499,000
	Apollo	\$30,315,000
	PCG	\$19,132,000
	Avenue Capital	\$18,586,000
Global Equity (Includes Corporate Governance)	Taiyo (Corporate Governance)	\$18,023,000
	Relational Investors (Corporate Governance)	\$10,873,000
	Arrowstreet Capital (External Equity)	\$7,169,000
	Genesis Asset Managers (External Equity)	\$5,891,000
	JP Morgan (External Equity)	\$5,741,000
Global Fixed Income	Pacific Investment Management Co.	\$1,861,000
	Mondrian	\$1,644,000
	Nomura Corp. Research	\$1,609,000
	Alliance Bernstein	\$680,000
	Rogge Global Partners	\$643,000
RMARS <sup>13</sup>	UBS	\$28,746,000
	Chatham Asset High Yield Offshore Fund, Ltd	\$23,488,000
	OZ Domestic Partners II, LP	\$19,363,000
	Black River Fixed Income Relative Value Opportunity Fund, Ltd	\$19,204,000
	PFM Diversified Fund, LP	\$19,168,000

## External Asset Management Expenses: Top 5 by Asset Class (2009 – 10), con't

Asset Class	External Manager/Partner	\$
ILAC	Timberland Timber Co.	\$9,152,000
	Alinda Capital Partners	\$8,274,000
	CIM Infrastructure	\$3,000,000
	UBS	\$2,500,000
	Carlyle Infrastructure Partner	\$1,500,000
Real Estate	LaSalle Investment Management	\$16,976,000
	CIM Group, LLC	\$15,273,000
	IHP Capital Partners	\$12,166,000
	Hines Interest	\$10,687,000
	Stockbridge Capital Group	\$9,577,000
Remaining External Management Expenses Total		\$646,612,000
<b>Grand Total</b>		<b>\$1,055,802,000</b>